MULTIMEDIA UNIVERSITY

STUDENT IDENTIFICATION NO

MULTIMEDIA UNIVERSITY

FINAL EXAMINATION

TRIMESTER 2, 2017/2018

BAC3624 – ADVANCED AUDITING

(All sections / Groups)

12 MARCH 2018
9.00 a.m – 12.00 p.m
(3 Hours)

INSTRUCTIONS TO STUDENTS

1. This Question paper consists of 5 pages excluding cover page with 5 Questions only.

2. Attempt all **FIVE** questions. All questions carry equal marks and the distribution of the marks for each question is given.

3. Please write all your answers in the Answer Booklet provided.

QUESTION 1

Your audit firm is the auditor for Sosa Medical Centre Sdn. Bhd., a manufacturer of dialysis equipment. You are aware that the company has recently designed a new dialysis machine with enhanced features, which market research indicates is likely to be very successful.

The development of the new dialysis machine has caused Sosa Medical Centre Sdn. Bhd. to run low on its cash flow. The managing director of Sosa Medical Centre Sdn. Bhd has written to the audit partner to see if the audit firm would be interested in making an investment in the new dialysis machine. It has been suggested that the auditors could provide finance for the completion of the development and the marketing of the new dialysis machine. The finance would be in the form of a convertible debenture.

Required:

i. Identify and explain the ethical implications in respect of the business arrangement with Sosa Medical Centre Sdn. Bhd.

(10 marks)

ii. Discuss the five fundamental principles of ethics as required by Malaysian Institute of Accountants' By – Laws (on Professional Conduct and Ethics) for its members to comply.

(10 marks)

(Total: 20 marks)

QUESTION 2

a) Expressing an independent opinion on the fairness of financial statements is the most important and valuable service rendered by the public accounting profession. The reporting phase begins when the independent auditors have completed their fieldwork and their proposed adjustments have been accepted and recorded by the client.

Required:

i. Under what circumstances may the auditor decide to include an "Emphasis of Matter" section in his audit report? (3 marks)

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ii. It is widely acknowledged that **materiality** is an important consideration in auditing. Discuss whether **'materiality'** is the only consideration for an auditor in deciding either to qualify or not for a financial report. (4 marks)

iii. What are the four (4) matters that need to be considered by the auditor before an unqualified report is being issued? (4 marks)

b) Haslin has prepared a letter of representation for the managing director and the financial controller to sign. It contains references to the following items:

- Inventory is fairly stated at the lower of cost or market and includes no obsolete items.
- All actual and contingent liabilities are properly included in the financial statements.
- All subsequent events of relevance to the financial statements have been disclosed.

Required:

i. Why is it desirable to have a letter of representation from the client concerning the above matters when the audit evidence accumulated during the course of the engagement is meant to verify the same information? (4 marks)

ii. To what extent is the letter of representation useful as audit evidence? Explain. (3 marks)

iii. List two (2) other types of information commonly included in a letter of representation. (2 marks)

(Total: 20 marks)

QUESTION 3

a) Due to rapid changes in information technology, most businesses utilized information system in their business operations. To keep abreast with the current development,

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auditors should update their knowledge and be competent when performing an audit in a computer information system (CIS) environment.

Required:

i. The use of a computer will change the processing, storage, communication of financial information and may affect the accounting and internal control systems employed by the entity. How would these changes affect the auditors in performing their audit? (3 marks)

ii. The auditors have to assess the inherent and control risk in the CIS environment. Explain the four (4) nature of risks and the internal control characteristics in the CIS environment. (8 marks)

b) After the auditor has completed the tests in specific audit areas, it is necessary to perform additional testing of a more general nature. This will include a review of subsequent events, review for contingent liabilities and accumulation of final evidence.

Required:

i. Define the two (2) types of subsequent events and give an example of each type. (3 marks)

ii. What would be the effect on auditor's report if a client failed to properly disclose the subsequent events? (2 marks)

iii. Explain the auditor's responsibility on facts discovered:

a. after the date of the audit report

b. after the financial statements have been issued. (4 marks)

(Total: 20 marks)

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QUESTION 4

Roller Coaster Bhd (RCB) is a public listed company, which was established in the year 2015 and have 88 stores all over Malaysia. The company focuses on selling shirts and pants. Supplies are purchased from approximately 28 different mid-sized local suppliers.

RCB has a well-staffed internal audit department, who report on a regular basis to the audit committee. Areas where the internal and external auditors may carry out work, include the following:

a) Attending the year-end inventory count in 22 stores annually. All stores are visited on a rotational basis.

b) Checking the internal controls over the purchasing systems (e.g. ensuring a liability is only recorded when inventory has been received).

Required:

a) For each of the above two areas, discuss the following:
   i. The objectives of the internal auditor. (6 marks)

   ii. The objectives of the external auditor. (6 marks)

b) Define corporate governance. Why do you think an effective internal audit function is essential to good corporate governance? (8 marks)

(Total: 20 marks)

QUESTION 5

You are working in a firm that performs an audit for Sosvin Berhad since 2010. The company manufactures designer handbags and does most of its business with Middle Eastern and European clients.

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In an effort to control the adverse currency exchange fluctuation, your audit firm in 2016 advised your client to set up a treasury unit to monitor the currency movements. Sosvin Berhad hired a new treasury executive, Nisa in January 2017.

In March 2018, when you were carrying out the audit of Sosvin Berhad for the year ended 31 December 2017, you found out that Nisa had entered into foreign exchange transactions without ensuring that the risk of adverse currency movement was properly evaluated.

On top of that, you also found that there were no supporting documents for these foreign currency transactions. When asked about the supporting documents, Nisa explained that she was given full authority to enter into these foreign exchange transactions and that she had produced an estimated profit for the company of RM 9 million.

You have brought these matters to the company finance director, Christina who assured you that Nisa's activities were genuine. Christina admitted that she did not monitor these transactions or review the documentation. Hence, Christina agreed to investigate the matter of the missing documentation and to make a disclosure regarding the company's involvements in foreign exchange transactions.

During the next audit in early 2019, you noted that the systems within the treasury unit had not improved since the previous year. Again documents could not be found and Nisa became worried when you questioned her. On the second day of the audit, Nisa disappeared and could not be contacted.

Upon investigation, you found that Sosvin Berhad had lost RM 50 million as a result of Nisa's speculation on foreign exchange markets.

Sosvin Berhad has instructed its lawyers to sue your audit company to recover their losses. The claim alleges that you negligently performed your contractual duties firstly by recommending that a treasury unit is established and secondly in failing to discover the fraudulent transactions.

Required:

i. Describe the arguments that you would expect to face from Sosvin Berhad's lawyers. (7 marks)

ii. Explain the points you could raise to defend yourself against the arguments identified in part (i) above. (10 marks)

iii. Briefly explain three responsibilities of the auditors with respect to detection of fraud. (3 marks)

(Total: 20 marks)

End of Paper